

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

In the Matter of)	
)	
Federal-State Joint Board on)	CC Docket No.
96-45		
Universal Service)	
)	
1998 Biennial Regulatory Review -)	
Streamlined Contributor Reporting)	CC Docket No.
98-171		
Requirements Associated with Administration)	
of Telecommunications Relay Service, North)	
American Numbering Plan, Local Number)	
Portability, and Universal Service Support)	
Mechanisms)	
)	
Telecommunications Services for Individuals)	CC Docket No.
90-571		
with Hearing and Speech Disabilities, and the)	
Americans with Disabilities Act of 1990)	
)	
Administration of the North American)	CC Docket No.
92-237		
Numbering Plan and North American)	NSD File No. L-
00-72		
Numbering Plan Cost Recovery Contribution)	
Factor and Fund Size)	
)	
Number Resource Optimization)	CC Docket No.
99-200		
)	
Telephone Number Portability)	CC Docket No.
95-116		
)	
Truth-in-Billing and Billing Format)	CC Docket No.
98-170		

COMMENTS OF NEXTEL COMMUNICATIONS, INC.

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SUMMARY

As the Commission reviews potential reform of its universal service assessment methodology it must consider first and foremost the impact of any such reform on *all* segments of the telecommunications industry. There is essentially one option for reform in front of the Commission – an IXC-proposed connection-based collection mechanism that substantially relieves IXCs of their universal service funding responsibilities. The case for this IXC-sponsored reform to the USF program has not been made. In today’s highly competitive marketplace, CMRS carriers are faced with a unique set of challenges, including intense price competition, closed capital markets, and highly elastic demand for wireless services. Continuing increases in surcharges and federal mandates has a direct, significant and harmful effect on CMRS carriers and thus on telecommunications competition.

As a matter of public policy, the Commission must make competitive neutrality and reasonableness the hallmark of its initiatives to reform universal service assessment mechanisms. The IXC proposal fails these tests. The IXCs’ connection-based assessment proposal, which is based on the unsupported premise that overall IXC revenue is eroding rapidly, unfairly shifts a large portion of USF contributions from IXCs and ILECs and their multiline business users to CMRS carriers. Further, under the proposed IXC “connection-based” plan, IXCs and ILECs together would contribute the \$1 monthly assessment for the landline connections they jointly serve, while CMRS carriers would be forced to shoulder the full \$1 per month assessment per activated handset. The proposed shift in USF burdens is inequitable and it is bad public policy. There is no justification, economic or otherwise, for allowing ILECs and IXCs to split USF costs

while requiring CMRS carriers to pay the full assessment amount. Competitive neutrality requires that each telecommunications carrier be assessed for the “connection” it provides.

Because the connection-based approach is flawed, it is fortunate that the Commission has other alternatives available. It could, for example, maintain the status quo as it works through other universal service proceedings. In addition, Sprint has made a proposal to freeze the current percentage of contributions by various industry segments and this could make sense as it would avoid a significant redistribution of the USF funding burden. Another approach would be to freeze CMRS carrier contributions at their 2001 level.

The Commission’s CALLS and MAG decisions, as well as the growth of USF-supported access lines due to consumers adding second and third lines in their homes, increase the amount of subsidies that have to be recovered from CMRS and other carriers prospectively. While encouraging affordable access to telecommunications services nationwide is a laudable policy goal, there are better ways to serve this goal than by continuing to increase the size of the USF by taxing at increasingly higher rates telecommunications carriers that compete with monopoly service providers. CMRS deserves special consideration because it is virtually the only source of possible facilities-based local exchange competition in the mass market. Of course, saddling CMRS providers with rapidly growing costs of monopolists could well prevent them from becoming the robust competitors their maturing networks could support.

The Commission has no easy choices in reforming universal service. The Commission must consider new approaches, such as freezing the amount of the federal USF fund. Certainly the growth in funding requirements on competitive carriers is unsustainable, and continuing

uncontrolled growth in USF funding requirements means that the base of potential fund contributors may have to expand.

To increase administrative simplicity for all industry segments, the Commission should consider having any flat rate USF assessment that it adopts mirror federal excise tax assessments. Administrative simplicity would be greatly enhanced if carriers could utilize a Federal Excise Tax model. Express application of the model would lessen carrier costs of litigation and substantially ease the burdens on carriers in assessing their USF contributions.

For all these reasons and given the current telecommunications market environment, there is little reason to consider broad-based revisions to the USF assessment program at this time. Instead, the Commission should focus efforts on reigning in the growth of the USF fund, so as not to discourage those entities and could provide competitive service alternatives to the mass market. One place to start may be by halting USF support for non-primary ILEC residential lines.

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COMMENTS OF NEXTEL COMMUNICATIONS, INC.

Nextel Communications, Inc. ("Nextel"), by its attorneys, hereby submits these
comments on the Further Notice of Proposed Rulemaking in the above-referenced proceeding.¹

¹ Federal-State Joint Board on Universal Service et al, *Further Notice of Proposed Rulemaking*, CC Docket No. 96-45; FCC 02-43 (rel. February 26, 2002) ("*Further Notice*").

The Federal Communications Commission's ("Commission") proposal to modify the universal service funding program should be rejected. The size of the funding requirement is growing rapidly and the assessments supporting it disproportionately burden Commercial Mobile Radio Service ("CMRS") providers financially and practically. The changes discussed in the *Further Notice* would be counter-productive – they would shift the burden of universal service recovery in a non-competitively neutral manner away from relatively inelastically demanded services such as landline local exchange service and the profitable multiline business market towards relatively elastically demanded services such as CMRS. The Commission should not adopt such an inefficient proposal. The better solution would be to maintain the current collection mechanism and take reasonable steps to limit the growth of the funding requirement.

Given the competitive, regulatory and current financial market environment facing CMRS and other telecommunications carriers, there is no pressing need to move to any new mandatory contribution assessment system, particularly to one that, without justification, precipitously shifts the burdens of mandatory cost recovery to CMRS customers. What the Commission must do is to freeze the dramatically growing burden of universal service assessments on CMRS providers at 2001 levels.² If, after careful analysis, the Commission decides to move toward a connection-based system, it must minimize the inefficiencies that will result by maintaining the relative contributions to the fund from various industry segments.

² The USF fund's contribution factor for the second quarter of 2002 is 7.28 percent, in contrast with the 3.19 percent assessment imposed on carriers end-user telecommunications revenue for the first quarter of 1998.

I. THE PROPOSED MODIFICATION IS NOT JUSTIFIED

Nextel is a national provider of CMRS services to approximately nine million domestic customers in the United States. Nextel is one of six facilities-based CMRS carriers whose commercial service offerings are considered national in scope. Because CMRS is highly competitive, largely unprofitable, possesses limited access to capital markets and has a nationwide penetration rate of only approximately 39%,³ imposition of additional universal service funding burdens on CMRS would be unsustainable, unwise and unlawful.

A. The CMRS Market Is Highly Competitive But Also Highly Challenged.

Nextel, along with the entire CMRS sector, continues to expand its geographic coverage throughout the United States and to introduce new services and competitive pricing plans for telecommunications as well as advanced services and features. This continuing expansion, requiring ongoing investment and reinvestment in networks and service, is taking place in a ferociously competitive CMRS market.⁴ The Commission generally recognizes these service, innovation and competitive pricing trends. As the most recent report on CMRS competition stated:

In the year 2000, the CMRS industry continued to experience increased competition and innovation as evidenced by lower prices for consumers and

³ See Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993; Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services, *Sixth Report*, 16 FCC Rcd 13350, fn 21 (2001) (“*Sixth Report*”).

⁴ According to one analyst “Government policy has made this competition a disaster, the government sucked capital out of telecom in a big way and created enormous disincentives for investment.” See Sandra Ward, *Stunted Growth, A Team of Tech-Telecom Specialists Sees More Static Ahead for Investors, Interview with Scott Cleland and William Whyman*, Barron’s Features (Feb. 25, 2002).

increased diversity of service offerings. The process of carriers building nationwide footprints continues to be a significant trend in the mobile telephone sector. The year 2000 saw a number of operators fill in gaps in their coverage through mergers, acquisitions, and license swaps. In parallel with the process of footprint building, mobile telephone operators continue to deploy their networks in an increasing number of markets, expand their digital footprints, and develop innovative pricing plans.⁵

This trend towards building out markets and offering new services has not only continued, but competition among CMRS providers has intensified as they vie to provide services that are responsive to consumer demand.⁶

All of this is occurring, however, at a time when capital markets are largely closed to the telecommunications industry. Like other CMRS providers, Nextel uses spectrum acquired in open markets or at auction in multiple markets to offer present and future services. All CMRS providers – with the exception of incumbent LEC cellular telephone company affiliates that were initially **given** their cellular licenses nearly two decades ago, and therefore operate with the benefit of a better, less debt-laden balance sheet – have already made enormous capital investment in spectrum infrastructure, handset equipment and marketing to develop competitive services. Due to the meltdown of many landline competitive LECs and other telecommunications service alternatives, CMRS now appears the only potential source of mass

⁵ See *Sixth Report* at 13353.

⁶ See, e.g., Sharon Pian Chan, *Merger Has Nice Ring for Wireless Firms*, SEATTLE TIMES, April 15, 2002 (noting that “competition has meant getting the lowest prices ever for wireless service, with most carriers enticing customers with no charges for long-distance calls.”); *Nationwide Plans Drive Costs Down*, COMM. TODAY, April 3, 2002 (noting that “competition among U.S. wireless carriers drove prices down 13 percent from October through March.”). Andrea Peterson & Nicole Harris, *Behind the Mayhem in Wireless Service*, WALL STREET JOURNAL, April 17, 2002, at 1 (noting that “[c]ompetition has cut rates and boosted minutes of use.”).

market local service competition: the competition the Telecommunications Act of 1996 contemplated and was supposed to encourage. Significant additional financial resources are required to acquire tower space, switching and base station equipment, to connect base stations to switches and to interconnect CMRS networks to other carrier networks. Some carriers may incur additional costs to relocate incumbent operators from newly licensed spectrum. There also are significant costs associated with providing even a single subscriber with CMRS service. These include subscriber handset subsidies, customer care support, engineering and back-office costs, the cost of billing and of necessary software and hardware improvements as well as the cost of state and federal regulatory and tax mandates. These are only some of the initial and continuing costs required to become a facilities-based CMRS service provider.

Like other CMRS providers, Nextel has had to raise billions of dollars in debt and equity to build out its network. Despite enormous success, and a growing and satisfied subscriber base, its business is not free cash flow positive and has not yet turned a profit. Moreover, as noted above, Nextel and other CMRS competitors must constantly invest and reinvest both to serve additional subscribers and to offer new services. This investment occurs while wireless service prices are declining in the highly competitive CMRS market.

All of these realities drive to the conclusion that the Commission should freeze – rather than increase – CMRS USF assessments because they limit subscribers’ purchases of CMRS services and burden carriers with costs at a time when capital markets are essentially closed and are largely hostile to the competitive CMRS industry. Moreover, recent bankruptcies of Competitive Local Exchange Carriers (“CLECs”) of all types and of satellite carriers, among others, have raised fundamental questions about the viability of competitive

telecommunications.⁷ Specifically, the many high-profile failures of new entrant CLECs and satellite competitors calls into question whether new entrants can successfully compete against incumbents that have enjoyed years of guaranteed rates of return on their investments, or that can absorb or cross-subsidize regulatory assessments among their subsidiaries or affiliates. These macro-factors are now a part of the policy mix the Commission must address and factor into its decision making.

B. Mandatory USF Contributions Have a Competitive Impact and the Joint IXC Plan Unacceptably Skews the Funding Burden.

Nextel is a mandatory contributor to the federal Universal Service Fund (“USF”). Nextel’s contributions to the USF have grown both as its subscriber base and as the quarterly contribution factors applied to all telecommunications carriers have risen. Like other CMRS carriers, Nextel has been forced by the highly competitive nature of the CMRS market to pass through its universal service mandatory contributions to its subscriber base. Nextel estimates the necessary contribution rate using a “percentage of revenues pass through formula” and currently applies a monthly line item charge uniformly across its entire customer base.⁸

CMRS providers are also mandatory participants in other state and federal regulatory and tax programs. Participation in these programs translates into additional fees that Nextel and other CMRS carriers must recover from their subscribers, either directly or indirectly. As

⁷ See Kevin Fitchard, *McLeod Bondholders To Decide: Little Now or Chapter 11 Later*, TELEPHONY, January 14, 2002; Michael Finneran, *New Values for New Times*, BUSINESS COMMUNICATIONS REVIEW, January 1, 2002; Jeffrey Silva, *The Big Hunt*, RCR WIRELESS NEWS, October 22, 2001.

⁸ Nextel monitors the fluctuations in the USF contribution factor and makes revisions to its USF line item charge periodically to avoid either under or over collection.

discussed above, the surcharges and costs of regulation that regulators impose affect the price of CMRS services significantly and can deter would-be subscribers from signing up for service.

Demand for wireless services is relatively elastic, compared to the relatively inelastic demand for primary line residential telephone service. This fact is critical in thinking about the proposed change to the universal service program. Historically, it has been inefficient to levy USF on relatively elastic interstate long distance revenues when the alternative was to tax the nearly completely inelastic demand for primary local exchange lines. But with CMRS and to a lesser extent, second residential lines, this relationship has changed. The “connections” at issue are no longer simply inelastic primary lines – they include elastically demanded CMRS services and second residential lines. Shifting a far greater funding burden to CMRS therefore will be inefficient in that it will create even larger marketplace distortions. Indeed, Nextel’s experience with universal service and other mandatory programs suggests that it is critical that the broad-based public policy goals underlying these programs be achieved without impairing competition, distorting markets or limiting consumer choices.⁹

The *Further Notice* requests comment on a particular proposal for reform of the current USF assessment mechanism. The fundamental thrust of the Joint IXC proposal is its shift of

⁹ Commissioner Martin echoed these concerns in his Separate Statement on the Notice of Proposed Rulemaking on Universal Service Obligations of Broadband Providers. He noted that taxes and fees of all sorts constitute financial burdens that could well discourage the deployment of broadband services and should be minimized. *See* Appropriate Framework for Broadband Access to the Internet Over Wireline Facilities; Universal Service Obligations of Broadband Providers; Computer III Further Remand Proceedings; Bell Operating Company Provision of Enhanced Services; 1998 Biennial Regulatory Review – Review of Computer III and ONA Safeguards and Requirements, *Notice of Proposed Rulemaking*, CC Docket Nos. 02-33, 95-20, 98-10, FCC 02-42 (2002). These same considerations apply with the greater force to CMRS services.

USF obligations away from IXC's and their multiline business users and towards CMRS.¹⁰ As discussed above, CMRS has a relatively high elasticity of consumer demand, and the shift of the USF funding burden as well as continuing expansion in the overall size of the USF fund will depress consumer demand for CMRS service and inject further economic uncertainty into the CMRS market. The proposal violates the statutory goals of neutrality and promoting competition.¹¹

In addition, the CMRS industry is already paying an increasing share of the universal service burden, an increase that is commensurate with the growth in the number of CMRS subscribers. This is because CMRS is growing rapidly compared to the local landline and long distance segments of the industry. However, the new subscribers to CMRS services are likely to be more price sensitive subscribers, choose lower priced service plans and because of these two factors, would be much more affected by a connection-based charge. A connection-based charge would lead directly to a higher percentage charge in the price for low end service (the service

¹⁰ Not only does the IXC proposal shift costs to CMRS users, but leaves business users to pay only the "residual" amount of USF assessment shortfall once the funding burden has been redistributed away from IXC customers generally. *See Ex Parte* Letter to Magalie Roman Salas, Secretary of the Federal Communications Commission, from Patrick H. Merrick, Director of Regulatory Affairs of AT&T Federal Government Affairs, AT&T Corp., CC Docket No. 96-45, *et al.*, at 1 (dated December 21, 2001) (discussing Coalition Proposal by Ad Hoc Telecommunications Committee, AT&T, e-TUG, and WorldCom).

¹¹ *See* 47 U.S.C. § 254(k) (requiring the Commission and States to establish regulations to ensure that no telecommunications service provider bears more than a reasonable share of the costs of ILEC facilities used to provide service); Federal-State Joint Board on Universal Service, *Report and Order*, 12 FCC Rcd 8776, 8801-02 (1997) (adopting competitive neutrality as a guiding principle for determining universal service support, and stating that "recognition of competitive neutrality in the collection and distribution of funds and determination of eligibility in universal service support mechanisms is consistent with congressional intent and necessary to promote 'a pro-competitive, de-regulatory national policy framework.'").

disproportionately chosen by lower income CMRS users). In addition, the higher price elasticity at the low end leads to a compounded market distortion of a reduced subscriber growth rate and higher prices for CMRS services.

Nextel submitted comments in June 2001 addressing the first Notice of Proposed Rulemaking in this proceeding.¹² Nextel's comments, among other things, urged the Commission to adopt a predictable flat fee assessment under which wireless providers would be assessed a per unit fee per activated mobile phone. Nextel's previous support for a flat fee approach was predicated on the assumption that any flat, per unit fee would not competitively disadvantage CMRS carriers vis-à-vis other market segments and would not include a vast increase in the share of USF funding borne by CMRS subscribers. Nextel's endorsement of a flat fee or unit assessment approach was aimed at eliminating the guesswork behind the fluctuation in the USF contribution factor and the delay between the reporting and collection periods. For the reasons discussed herein, however, Nextel opposes the IXC connection-based and industry-shifting assessment plan.

While Nextel favors administrative simplicity, developing a competitively neutral mechanism to simplify current universal service collection procedures is a difficult objective to achieve and is worthy of deliberate Commission action. If, after careful consideration, the Commission determines that some form of a unit-based assessment system better serves the public interest than the current revenue-based system, it is imperative that the assessment method be competitively neutral as among industry segments and as between competitors in a

¹² Comments of Nextel Communications, CC Docket Nos. 96-45, 98-171, 90-571, 92-237 (NSD File No. L-00-72), 99-200, and 95-116 (filed June 16, 2001) ("Nextel Comments").

competitive industry segment. Indeed, reform of the current USF methodology should not center on shifting funding burdens from one segment of the telecommunications market to another.

Instead, the Commission should seek to adopt a program that will reduce the USF burdens on all carriers in a manner that avoids cross-subsidization and the creation of regulations that favor one industry segment, or subsegment, over another. The Commission's responsibility under the law and its proper focus should be on managing the increasing size of the fund responsibly to lessen the distortion that the USF contribution already has on competitive markets.¹³

II. THE CASE FOR CHANGE IS NOT CONVINCING

Nextel is in favor of administrative simplicity for USF assessments when simplicity can be fairly and reasonably determined and applied, and when competitive neutrality can be achieved. That being said, the case for fairness and competitive neutrality of the Joint IXC proposal for USF funding has not yet been made.

A. Overall IXC Revenue Is Not Eroding.

The *Further Notice* requests comment on "replacing the existing system with a connection-based assessment."¹⁴ In particular, it asks whether the Commission should assess universal service contributions based on the number and capacity of connections a carrier

¹³ See *AT&T Corporation, et al. v. Iowa Utilities Board et al*, 525 U.S. 366 (1999) ("Since Congress expressly directed that the 1996 Act, along with its local-competition provisions, be inserted into the Communications Act of 1934, 1996 Act, Section 1(b), 110 Stat. 56, the Commission's rulemaking authority would seem to extend to implementation of the local-competition provisions."). Thus, it would follow that the Commission's universal service rules and procedures should not operate to benefit one class of carriers over another and thereby distort competition in local telecommunications markets.

¹⁴ *Further Notice* at ¶ 15.

provides to the public network. This proposal has been strongly promoted by much of the IXC industry as well as by trade associations representing multiline business users. Alleging that they are locked in a “world of declining interexchange carrier revenues,” the Joint IXCs that originally submitted the proposal claim that absent the adoption of their proposal, the current system will “inevitably lead to a USF ‘death spiral.’”¹⁵ However, their support for this plan simply demonstrates that they would benefit as other market segments (and customers of those segments) are forced to shoulder the USF funding burden being shed by IXCs and large businesses.

The Joint IXCs have nothing beyond their own apocalyptic statements to demonstrate that the current USF system is unstable and in immediate need of salvation via a wholesale change of the assessment mechanism. Indeed, the IXC predicate for wholesale change, in essence, is that competition in the long-distance marketplace is forcing a decline in IXC revenues.¹⁶ Yet the facts do not support that proposition. The IXCs own revenue figures indicate at most a slight decline in IXC revenues over the past three years.¹⁷ Indeed, Sprint’s

¹⁵ Comments of WorldCom, Inc., CC Docket No. 96-45, *et al.*, at 11 (filed June 25, 2001) (“WorldCom Comments”); *see also Ex Parte* Letter to Magalie Roman Salas, Secretary of the Federal Communications Commission, from Patrick H. Merrick, Director of Regulatory Affairs of AT&T Federal Government Affairs, AT&T Corp., CC Docket No. 96-45, *et al.*, at 1 (dated December 21, 2001) (discussing Coalition Proposal by Ad Hoc Telecommunications Committee, AT&T, e-TUG, and WorldCom).

¹⁶ *See, e.g.*, WorldCom Comments at 2-3 (asserting that “market developments have reduced traditional interstate telecommunications revenues and made it increasingly difficult to identify and measure the ‘new’ interstate telecommunications revenues, thus rendering the current narrow assessment base insufficient to sustain the USF in the long run.”).

¹⁷ *See* Exhibit 1 (IXC Revenue Chart).

most recent reported interexchange revenue figures suggest that there is no significant erosion in its interexchange revenues.¹⁸ Even if it were true, however, that some IXC's cannot realize the same revenues per minute of use as in the past, the same is true for CMRS providers in an increasingly competitive CMRS market segment. Thus, it is certainly no reason for providing specific USF funding relief to IXC's.

One possible cause for potentially declining revenues among some of the traditional interexchange carriers is the entry into the interexchange market of the Bell Operating Companies ("BOCs"). Traditional interexchange carriers' market shares are under challenge in states where BOCs have received the requisite Section 271 interLATA service authority.¹⁹ And while there may be a time lag between the time a BOC enters the interLATA market and it reports and pays USF assessments on its revenues, the case for "declining" IXC industry revenues has failed to account for the shift of some portion of interexchange revenues from traditional interexchange carriers to the BOCs that have received or shortly may receive interLATA service authority.²⁰

¹⁸ In fact, Sprint's revenues were better than some analysts expected. Sprint's revenue was \$4 billion, down from \$4.3 billion in previous years. COMM DAILY, April 17, 2002, at 3.

¹⁹ Hearing of the House Judiciary Committee; Subject: Broadband Competition; Testimony of John Malone, President And Chief Executive Officer, The Eastern Management Group, Bedminster, New Jersey. Mr. Malone stated that "271 relief in any state probably is a free ticket to about a billion dollars of additional revenue for a regional Bell." See also COMM. DAILY, July 21, 2000 (noting that "[b]esides wireless, SBC clearly sees data and long-distance as its 2 big revenue drivers. [The] Tex[as] long-distance market is worth \$7.7 billion alone and Cal[ifornia] will top \$15 billion by the time [the] ILEC gets Sec. 271 approval [and] [l]ong distance is a great example of growth at SBC.").

²⁰ To the extent IXC's can demonstrate that some portion of their revenues are disappearing because of the growth of Internet Protocol telephony, then they may have a reason to seek to
(continued...)

The Commission cannot accept at face value IXC assertions about declining revenues and use them to modify USF assessment requirements. Neither the actual magnitude of the purported decline in traditional IXC revenues, nor the rapidly growing BOC IXC revenues, seem to be reflected in the Joint IXC plan or in the analysis of the Joint IXC plan in the *Further Notice*. One simple solution to any shift in interstate revenue from the IXCs to the BOCs is to use a prospective USF assessment with a subsequent “true-up.” It is hard to argue that because of “increasing competition” in interstate long distance services that IXCs should be allowed to escape an industry universal service fee and then put that burden squarely on the shoulders of another competitive sector.

Beyond the threshold issue of the absence of a factual predicate necessitating a major overhaul of the USF assessment system, the Commission must also address whether the proposed connection-based mechanism would result in the equitable collection of universal service funds from all carriers, and whether it has the appropriate legal authority to implement such a mechanism.²¹ These issues should not be taken lightly and a complete overhaul of the USF assessment program should not be conducted and new rules adopted without careful consideration of whether such overhaul truly is necessary, including whether there are other less disruptive alternatives available.²² In this instance, where there are far less disruptive

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have the Commission to expand the pool of potential USF contributors to include IP telephony providers.

²¹ See *Further Notice* at ¶ 65 (seeking comment on whether a connection-based assessment satisfies each element of the requirement in Section 254(d) of the Act).

²² While the scope of judicial review under the arbitrary and capricious standard is narrow, reviewing courts still ensure that agencies take a “hard look” at all relevant issues and consider
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alternatives to a connection-based assessment approach, the Commission has a high hurdle to justify changing its assessment program in a manner that exacerbates competitive neutrality problems and harms potential ILEC competitors.

Preliminary Commission staff analysis suggests that the “total” contribution recovery fees paid by an “average” household under a connection-based system would be approximately \$1.93, purportedly the same as under the existing system.²³ Assuming for purposes of argument that this preliminary analysis is correct, it illustrates a grave problem with the IXC plan. The \$1.93 average recovery analysis assumes a landline and a mobile connection in the majority of homes. Of course, many homes have second lines and families with two working parents have “family plan” CMRS services with several cell phones to keep in touch with their children when they are at work. These households would be disproportionately harmed by the proposed shift in the assessment base. For example, if a family had two landline connections and CMRS family plan service for four handsets, that family’s USF costs would total \$6, not \$1.93.²⁴ Thus, while an “average” household might theoretically not pay more than under the change in USF assessment method, many other households would pay more.

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all reasonable alternatives and relevant factors. *See Neighborhood TV Company, Inc. v. Federal Communications Commission*, 742 F.2d 629 (D.C. Cir. 1984). Further, the FCC cannot escape judicial review of wholly arbitrary action by merely instituting a waiver procedure that would allow it to correct in the future the arbitrary results of its actions. *Alltel Corporation v. Federal Communications Commission*, 838 F.2d 551 (D.C. Cir. 1988).

²³ *Further Notice* at ¶ 46.

²⁴ The family would pay \$1 for each landline connection and \$1 for each activated CMRS handset.

This average household analysis also does not highlight that, under the IXC proposal, incidence of USF taxation is being shifted from IXCs, and to a degree, from ILECs, as they would jointly contribute \$1 for a landline connection they jointly serve, while mobile connections would be assessed a full dollar per activated handset each month. The CMRS industry, already under great financial challenge, would be asked to shoulder a huge additional and increasing burden. As discussed herein, the conclusion that this should not particularly matter because the USF assessment is passed onto subscribers is mistaken, because CMRS and other landline services do not exhibit similar degrees of market penetration, profitability or elasticity of demand. An increase in CMRS rates will adversely affect CMRS carriers' ability to compete in the local telecommunications market against the monopoly ILECs, ironically the very market being subsidized using the mandatory assessments imposed on CMRS.

B. There Is Potential Instability in any Tax or Assessment Program; the Key to Managing the Program is to Manage Growth in Funding Requirements.

The Commission's fundamental concern expressed in its *Further Notice* is its frequently-stated concern about the long-term stability of the Universal Service Fund. It is important to recognize, however, that the Commission would continue to have the same funding stability concern under the proposed new system. For example, if there are declining numbers of assessable connections, USF funding would be no more stable. The effective tax rate on individual carriers and on market segments would still fluctuate. Thus, before the Commission adopts any specific proposal, it must focus on the most fundamental issue at hand, *i.e.*, how to mitigate the harmful effects of a subsidy program that distorts competitive markets like CMRS by looking at both USF contribution and USF distribution effects.

For instance, USF distributions aid only one service provider: the subsidized provider has a ready means of setting its prices below its costs while retaining or increasing its profitability.²⁵

Such below-cost pricing becomes an effective barrier to competition because potential competitors, who are not entitled to receive a subsidy or who receive less of one, will be discouraged from entering the market or being able to compete even if they are more efficient – because they cannot price below the subsidized price – and even though they may be able to provide the services at a cost less than the subsidized provider’s cost.²⁶

The key, therefore, is for the Commission to resist any further USF subsidy increases so that the funding base does not grow unreasonably large and to consider new ways to police the fund’s current size. Unmanaged growth in USF funding requirements stimulates uneconomic investment by the entities receiving the subsidy at the expense of the growth and development of companies building networks, facing closed capital markets and intense competition. Much closer attention needs to be paid to this linkage. Otherwise, our nation’s tenuous competitive

²⁵ See, e.g., Richard Posner, *ANTITRUST LAW: AN ECONOMIC PERSPECTIVE* 187-88 (1976). Posner has argued in the context of predatory and discriminatory pricing that “the misallocative effects of a firm’s selling a product below cost, thus inducing inefficient substitution toward it, are not reduced by its subsequently selling the product at a monopoly price and thus inducing substitution away from it.” Moreover, “[a] subsidy designed to enable a firm to sell its product at a price below marginal cost produces the same distortion as monopoly power that enables it to sell the product above cost: the subsidy and resulting price change attract consumers from products that are socially less costly to produce, just as monopoly pricing deflects consumers to products that are socially more costly to produce.” Richard Posner, *ECONOMIC ANALYSIS OF LAW* 309 (4th ed. 1992).

²⁶ See, e.g., *International Settlement Rates, Report and Order*, 12 FCC Rcd 19806, 19902-03 (1997) (explaining, in the context of the *International Settlements* proceeding that “where the U.S. affiliate sets its prices *below its own costs* of providing service, the lower prices may be the result of a predatory price squeeze and distort competition.”) (emphasis added).

experiment in the wireless industry segment will be undermined and a serious decline in competition will result.

The *Further Notice* should not merely be an inquiry into how to provide USF payment relief to IXC's. All competitive carriers are financially constrained, with CMRS carriers more so than ILECs or IXC's.²⁷ No one industry segment should have to bear a heavier burden of USF taxation than it does currently. The Commission instead should be striving to lessen the contribution load on all carriers. In any event, the Commission must engage in a probing review of the amount that is required to be collected, the collection method that is the most equitable, and the formula that accomplishes these objectives. The Commission cannot uncritically accept the IXC proposal without doing this analysis.²⁸ Indeed, the Commission should ask whether it promotes the public interest to impose these burdens to support second or third lines in beneficiary markets given the price competitors and their customers are called upon to pay.

III. THE JOINT IXC PROPOSAL UNIQUELY ADVANTAGES THAT INDUSTRY

Under the Joint IXC proposal "residential, single-line business, and mobile wireless connections (excluding pagers) would be assessed a flat amount of \$1.00 per connection," while multiline business users would face a substantially reduced residual recovery amount.²⁹ The proposal also would allow IXC's and ILECs to "split" the \$1 assessment between them, assuming

²⁷ See Heather Forsgren Weaver, *Senate Staffer: If Wireless LNP is Delayed Other Requirements Should Be Included*, March 11, 2002 (noting that the CMRS industry is saddled with several additional federal mandates than landline carriers).

²⁸ *American Trading Transp. Co. v. U.S.*, 791 F.2d 942, 948 (D.C. Cir. 1986) (holding agency action invalid where there was no evidence that the agency considered its statutory goal).

²⁹ *Further Notice* at ¶ 31.

that they share the same residential service connection, further lowering the IXC and ILEC funding obligation. This proposal cannot be adopted, as it unfairly advantages particular market segments at the expense of other market segments.

A. The Joint IXC Plan Shifts the Funding Burden Away from their Most Favored Customers.

As an initial matter, there has been no demonstration that a monthly assessment of \$1.00 per month per connection has any foundation in law or policy. In fact, \$1 per connection would represent a huge increase in assessments to CMRS users, who, according to the *Further Notice*, now pay less than half that amount. To double the amount of tax on one segment of the industry while lowering it on others, particularly multiline business customers who may have a lower elasticity of demand for their landline services and greater ability to pay, is bound to create distortions and inefficiencies.

Further, there has been no explanation of the legal and public policy justifications for leaving only a drastically reduced “residual” USF funding burden on multiline business users once the bulk of the assessments have been shifted to a connection-based fee collected from single line telephone subscribers and CMRS subscribers. It also appears to violate Section 254(k)’s direction that non-competitive services may not subsidize competitive services. Plainly there is more competition in the multiline business market than in the landline local exchange market.³⁰ The statute directs that a “telecommunications carrier may not use services that are not

³⁰ See Joint Applications of Telephone and Data Systems, Inc. and Chorus Communications, Ltd. for Authority to Transfer Control of Commission Licenses and Authorizations Pursuant to Sections 214 and 310(d) of the Communications Act and Parts 22, 63 and 90 of the Commission's Rules, *Memorandum Opinion and Order*, 16 FCC Rcd 15293, 15297-15298

(continued...)

competitive to subsidize services that are subject to competition.”³¹ The underlying purpose of Section 254(k) is to prevent carriers from attempting to gain an unfair advantage in competitive markets by allocating to their less competitive services, for which subscribers have few or no available alternatives, an excessive portion of the costs incurred by their competitive operations.”³² The Commission must ensure that the Joint IXC proposal does not shift the burden of funding from the most competitive part of the IXC market, the multiline business segment, to other business segments in contravention of statutory requirements.

The *Further Notice* seeks comment on whether and how a connection-based USF assessment mechanism would work for multiline business connections. If “a connection is a connection” and no consideration is given to the relative capacity of the connection, then “single line” connections and CMRS “connections” will be assessed far more than previously and multiline business connections will be unjustifiably advantaged by shedding millions of dollars of USF funding obligations. Even assuming a capacity-based charge is imposed, the Joint IXC proposal fails to provide crucial details such, as the possible revenue

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(2001) (stating that the Commission has recognized that “business customers, in particular larger businesses, generally face more competitive choices than residential customers.”).

³¹ 47 U.S.C. § 254(k). To prevent such cross-subsidization of services, the Act also requires that the “Commission, with respect to interstate services, and the States, with respect to intrastate services, shall establish any necessary cost allocation rules, accounting safeguards, and guidelines to ensure that services included in the definition of universal service bear no more than a reasonable share of the joint and common costs of facilities used to provide those services.”

³² Tennessee Cable Telecommunications Association, et al., and Cable Television Association of Georgia, *et al.*, Complainants, v. BellSouth Telecommunications, Inc., *Memorandum Opinion and Order*, 15 FCC Rcd 7513, 7516 (2000).

impact on USF; the effect of freezing a connection-based assessment at \$1 as the *Further Notice* suggests; rules for calculating capacity or connection-based equivalent charges on multiline business connections; and the reasonableness *ab initio* of any connection-based assessment regime.

In addition, under the Joint IXC proposal, IXCs and ILECs would pay substantially less to support the USF as compared to other carriers, such as CMRS providers, that typically offer bucket plans with local and long distance component services in a bundle. Indeed, using the assumption that they together serve a single customer connection, IXC plan takes the approach that IXCs and ILECs should “split” the \$1 monthly connection assessment between them. Each would be assessed half of what a CMRS carrier would be assessed.

The Commission ought not to punitively assess higher charges on bundled wireless service offerings, particularly under the purported view that a “connection is a connection scheme” somehow simplifies the USF contribution mechanism. To maintain even the semblance of competitive neutrality, each provider must be assessed for the “connection” it provides, so long as it can be established that connections are defined to ensure a fair allocation of assessments to the fund. Any other approach to defining connections would place wireless at an enormous financial disadvantage and would not be competitively neutral.

B. There Are Reasoned Alternatives to a Connection-Based Assessment Regime.

Interestingly, and in contrast to the Joint IXC proposal, Sprint has submitted a plan to modify the USF contribution mechanism.³³ Sprint serves all the major telecommunications market segments – local, IXC and CMRS. As such, it may well have a broader understanding of how the USF mechanism must be adjusted to alleviate the financial and administrative burdens of all carriers. In particular, Sprint proposes to freeze the relative contributions of various industry segments as they are today and thus avoid a potentially significant redistribution of the funding burden. In addition, Sprint argues that major changes to the USF contribution mechanism should be delayed until the Commission has determined the best method for all carriers.

In support of its proposal, Sprint correctly points out that there is more stability in the industry generally than other IXCs portray and that a hasty overhaul of the USF assessment mechanism is inappropriate at the present time.³⁴ Further, Sprint suggests that the outcome of pending Supreme Court cases and other ongoing USF litigation could bear heavily on the effectiveness of the USF program. Judicially ordered modifications could well necessitate revisions to the entire federal universal service program.³⁵ Sprint's suggestions make sense.

³³ See *Ex Parte* Letter to Magalie Roman Salas, Secretary of the Federal Communications Commission, from Pete Sywenki, Director of Federal Regulatory Affairs for Sprint (filed August 8, 2001) (“Sprint Proposal”).

³⁴ See Sprint Proposal.

³⁵ See, e.g., *Iowa Utils. Bd. v. FCC*, 219 F.3d 744 (8th Cir. 2000); *cert. granted sub nom., Verizon Communications v. FCC*, 531 U.S. 1124 (2001). Last fall, the Supreme Court heard oral argument on a number of issues centering on the cost methodology adopted by the Commission for determining the rates that new entrants into local telecommunications markets must pay

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Awaiting the outcome of these pivotal events affecting the federal universal service fund is more sensible than putting in place a dramatically new program that may have to be fully revamped within the next few months.

Sprint also raises concern that the Commission's prior findings approving an interstate revenue-based USF assessment method should not be overturned without a record and justification for change consistent both with the statute and the public interest.³⁶ In reforming the contribution and collection process, the Commission must "balance the interests of the primary contributors to the fund: the public and three carrier segments: local exchange carriers ("LECs"), interexchange carriers ("IXCs") and Wireless carriers."³⁷ In addition, the Commission must design a program that meets the "goals of adaptability, competitive neutrality and simplicity."³⁸ Realizing these goals will not be easy and the Commission should establish a process that is likely to produce this result.

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ILECs. Also under consideration is whether the lower court erred in holding that neither the Takings Clause nor the Telecommunications Act of 1996 requires incorporation of an ILEC's "historical" costs into the rates that it may charge new entrants for access to its network elements. These are major issues affecting carrier rates and the Supreme Court's ruling on these issues could have a tremendous effect on ILEC rates, and thus the amount of revenues received by these carriers for their services. *See also* *Qwest Corp. v. FCC*, 258 F.3d 1191 (10th Cir. 2001). There the Tenth Circuit reversed and remanded the Universal Service *Ninth Order* because it failed to provide adequate reasoning for the established funding mechanism to support universal service and why the funding is "sufficient," as required under the statute, to support the program. The outcome of this proceeding will effect the level of funding of the program.

³⁶ *See* Sprint Proposal.

³⁷ Reply Comments of Sprint Corporation, CC Docket No. 96-45, *et al.*, at 3 (filed July 9, 2001).

³⁸ *Id.*

Another proposal worth considering is one that freezes CMRS carrier contributions at their 2001 levels until the Commission has the opportunity to consider reforms in USF assessment policy not in a vacuum, but in connection with necessary USF distribution reforms aimed at limiting the size of the fund. Now is not the time to impose additional taxes on CMRS, for the reasons previously discussed. One way to make up any potential funding shortfall is reflected in the *Further Notice* and is worthy of further consideration – expansion of the pool of USF contributors beyond traditional telecommunications carriers.³⁹

IV. DEMAND FOR WIRELESS SERVICE IS GROWING, BUT THIS DEMAND IS NOT INELASTIC

An important factor to consider when modifying the USF contribution mechanism is that carrier networks, economics and operational characteristics differ radically and changes in the effective rate charged to consumers for CMRS service have a different impact on demand for CMRS services than would a similar change in the effective rate for local landline service, for example. In considering revisions to the collection and contribution mechanism, the Commission cannot overlook the importance of the different elasticity of demand for service in different segments of the telecommunications market. Regulation and government fee collection programs should not force every company to wear the same shoe – not all companies have the same foot size.

³⁹ *Further Notice*, at ¶ 4. In the *Further Notice*, the Commission has initiated another proceeding that explores the universal service obligations of providers of facilities-based broadband Internet access. The Commission advised commenters to be mindful of the relationship between this proceeding and the other proceeding and, where appropriate, to address interrelated issues raised by the proposals. See Federal-State Joint Board on Universal Service, *Notice of Proposed Rulemaking*, 16 FCC Rcd 9892 (2001).

In the competitive wireless marketplace, for instance, carrier networks, technologies and economics differ in significant ways. As the Commission recently said “[o]f the six nationwide mobile telephone operators, Sprint PCS and Verizon Wireless have CDMA as their digital technology, AT&T Wireless uses TDMA, VoiceStream uses GSM, and Nextel uses iDEN. Cingular Wireless has a mix of TDMA and GSM networks.”⁴⁰ Further, these carriers target their services to different markets, such as casual users, prepaid users, family service plans, business users and the like. Based on volume of orders, both infrastructure and handset prices can vary widely. Carriers also, of course, have very different embedded costs of spectrum and capital.

The Commission did not intend that CMRS – or even the telecommunications market as a whole – be, or become a one-size fits all industry. Any regulation that ignores this would constitute arbitrary and capricious decision making and would undermine the very competition the Commission, through other policies, has sought to encourage.⁴¹ Rather, the Commission has expressly encouraged CMRS carriers to develop different technologies, to target different market segments or niches, to provide a rich cornucopia of advanced, value-added communications for

⁴⁰ *Sixth Report*, 16 FCC Rcd at 13367-68.

⁴¹ *See, e.g.*, Interconnection and Resale Obligations Pertaining to Commercial Mobile Radio Services, *First Report and Order*, 11 FCC Rcd 18455, 18464 (1996) (applying the resale rule only to specific services, and concluding that “considerations of parity do not require identical regulation of services that are differently situated. Indeed, in determining whether carriers in different services should be subject to similar regulations, we have consistently examined whether they were similarly situated with respect to, among other factors, the markets they serve.”) (citations omitted).

people on the go.⁴² The additional cost of existing mandates and explicit taxes on CMRS is very significant. CMRS operates in a highly competitive market in which carriers cannot simply “absorb” their staggering costs.⁴³

Mandate costs in whole or part are passed on to wireless consumers, including line item charges for E-911, local number portability and USF. These taxes, surcharges and subsidies affect consumer behavior.⁴⁴ Indeed, consumers respond to price reductions for services offered

⁴² See Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993; Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services, *Third Report*, 13 FCC Rcd 19746 (1998) (noting that “[t]elecommunications devices exist today that were not imagined only a few years ago. The Commission does not wish to impose regulations that will slow the emergence of new, innovative technologies[for consumers]. As a result, the Commission has been moving forward with policies that afford licensees the flexibility necessary for the marketplace to determine the appropriate spectrum uses”).

These points tend to be overlooked in the application of regulatory mandates, however. E-911, USF, CALEA and local number portability, to name a few, are applicable to all CMRS providers regardless of their size, customer penetration, or ability to fund these mandates. Furthermore, the Commission consistently attempts to apply one-size fits all regulation and cost assessments irrespective of the differing competitive impacts of such mandates on vastly different carrier technologies and economics. The Joint IXC plan would do just the same.

⁴³ See, e.g., *FCC Order on CALEA Remand Keeps Surveillance Requirements Intact*, COMM. DAILY, April 12, 2002 (noting that “FCC Commissioner Copps expressed concern that CALEA-related costs for those mandates would be high for residential customers and *wireless carriers*, particularly rural providers) (emphasis added). While some carriers can absorb these costs, because of their profitability owing to long-time incumbent status, other competing CMRS carriers cannot and must pass them on to their customers.

⁴⁴ Hearing of the House Ways and Means Committee; Subject: Proposals To Reduce Taxes; Testimony of J.D. Foster, Executive Director and Chief Economist of the Tax Foundation (February 4, 1998) Mr. Foster discussed the effects of tax cuts on consumer behavior:

This committee has heard for years that Americans save too little. Assuming this is true, our marginal tax rates must bear much of the fault. People respond strongly to incentives and disincentives. Why do you suppose brokerage houses
(continued...)

in the market.⁴⁵ Because local landline residential telephone service is inelastically demanded by consumers – consumers tend to accept additional taxes and surcharges on those services without changing their basic behavior – they continue to be landline telephone subscribers. However, in the CMRS market, where wireless service is not considered essential, and consumers readily switch providers, consumers exhibit far greater elasticity of demand.

Continuing increases in surcharges and mandates has a harmful effect on relative subscription rates and market development. Certainly, the rate of growth in CMRS subscribership has slowed in the last few years, despite intense price competition among CMRS carriers.⁴⁶ Failure to account for this relative demand elasticity will result in a failure to acknowledge that government mandates and the regulations implementing them can become a source of competitive advantage or disadvantage, potentially benefiting one industry, but harming the public interest through a diminution in competition.

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advertise track records of yielding values to investors if investors are not swayed by yields? Why do super markets advertise their prices in the local paper? Because even reduction in the price of a can of soup or a bunch of bananas is going to alter consumers' behavior.

⁴⁵ Prepared Testimony of John S. Fitzpatrick Executive Director Mergers and Acquisitions Touch America, Inc. Before The Senate Commerce Committee Subcommittee On Communications (March 28, 2000) (as the prices of advanced broadband capabilities continue to decline, “access to, and the use of, such services will increase.”).

⁴⁶ “After years of rapid expansion, the industry’s growth peaked in 2000, when 23.4 million new subscribers signed up for wireless service. That number slid to 20.6 million in 2001 and is expected to fall to 17.1 million in 2005.” Andrea Peterson & Nicole Harris, *Behind the Mayhem in Wireless Service*, WALL STREET JOURNAL, April 17, 2002, at 1.

In light of the existing costs faced by the wireless industry, Nextel's support of a move to any connection-based assessment mechanism would be premised on the assumption that the Commission will not permit the proposed arbitrary loading of additional costs onto CMRS – the only viable, facilities-based mass consumer alternative to ILEC local services. If the Commission determines that a connection-based system better serves the public interest than the current revenue-based system, it is imperative that the fees assessed be competitively neutral and take into full account the relative elasticity of demand for various telecommunications services. In particular, any modified assessment plan should not upset the current relative balance of USF payments as among industry segments.

V. ANY FLAT RATE USF ASSESSMENT SHOULD MIRROR TRANSACTION-BASED ASSESSMENTS, SUCH AS FEDERAL EXCISE TAX ASSESSMENTS

In any reform the Commission ultimately adopts, it should strive to achieve administrative efficiency and to reduce the administrative burdens on carriers. Administrative simplicity would be greatly enhanced if carriers could utilize a Federal Excise Tax model as their USF collection model. Indeed, the Federal Excise Tax model is a well established tax model that can be easily applied. Moreover, the excise tax program recognizes exemptions from assessments due to basic public policy reasons based on the tax status of certain entities such as state and local government entities.

Under the current Federal Excise Tax regime, a three percent telephone tax is imposed on the amounts paid for local telephone service, toll telephone service, prepaid telephone cards and teletypewriter exchange service. Nextel *does not* suggest the application of a three percent USF rate; it is the methodology of application of charges under the Federal Excise Tax model that is relevant to this proceeding. The tax is imposed on the person paying for the telephone services

and the person receiving payment for the services is required to collect the tax, pay it to the federal government and to file returns. Importantly, the telephone excise tax exempts certain entities for the tax on the services they purchase, including services provided to the government of any state, the District of Columbia, nonprofit hospitals, and to certain news services or nonprofit educational institutions.

The exemption for state and local governments from payment is not unlike the public policy exemption currently made to USF contributions for Lifeline telephone subscribers. Under the existing system, ILECs may not recover universal service contributions from their Lifeline subscribers.⁴⁷ Further, Nextel's experience suggests that some state and local government customers may be contesting their obligation to pay federal USF charges and using this as leverage in contracting with carriers that agree not to pass USF charges on to them. If this trend continues, it raises the prospect of carriers discriminating in favor of state and local government customers. Application of a Federal Excise Tax model as the USF collection model would allow this discrimination as being consistent with public policy, lessen carrier costs of litigation, create a more neutral competitive environment and eliminate the administrative burdens.

⁴⁷ See 47 C.F.R. § 69.158; *see also* Access Charge Reform, *Sixth Report and Order* in CC Docket No. 96-262 and 94-1, *Report and Order* in CC Docket No. 99-249, *Eleventh Report and Order* in CC Docket No. 96-45, 15 FCC Rcd 12962, 13057-58 (2000); Multi-Association Group (MAG) Plan for Regulation of Interstate Service of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers, CC Docket No. 00-256, *Second Report and Order*, Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Fifteenth Report and Order*, Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation, CC Docket No. 98-77, *Report and Order*, Prescribing the Authorized Rate of Return for Interstate Service of Local Exchange Carriers, CC Docket No. 98-166, *Report and Order*, 16 FCC Rcd 19613, 19688-89 (2001) ("Multi-Association Group Order").

Finally, while the *Further Notice* appears to suggest that the Commission may expect carriers that collect a dollar of USF support to simply remit the full dollar to the Commission's USF Administrator, there are carrier-specific costs of administering the assessment program and these costs will not be eliminated by a move to connection-based charges. Thus, the Commission must allow administrative expense recovery for carriers administering federal USF. Many states and many state E911 cost recovery surcharge programs use this practice.

VI. THE COMMISSION'S FOCUS SHOULD BE ON CONTROLLING THE GROWTH OF THE USF FUNDING REQUIREMENT

There should be no question that USF funding requirements can distort competitive markets and funding requirements should be set at the absolute minimum to achieve the stated goals of the statute. There have been a variety of regulatory decisions made in the last several years that have increased the size of the USF fund, particularly the Commission's decision in the CALLS proceeding to redesignate \$650 million of ILEC annual interstate access revenue as a universal service subsidy and the MAG decision, in which carriers that all benefit from USF subsidies persuaded the Commission to shift costs to the USF program. These initiatives unquestionably have increased the amount of subsidies that have to be recovered from CMRS and other carriers.⁴⁸ Other proposals on the horizon include considering access to the Internet or

⁴⁸ Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, CC Docket Nos. 96-262 and 94-1, *Sixth Report and Order*, Low-Volume Long-Distance Users, CC Docket No. 99-249, *Report and Order*, Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Eleventh Report and Order*, 15 FCC Rcd 12962 (*CALLS Order*), *aff'd in part, rev'd in part, and remanded in part*, *Texas Office of Public Util. Counsel et al. v. FCC*, 265 F.3d 313 (5th Cir. 2001).

to broadband facilities as services to be funded by USF.⁴⁹ If the Commission believes that it is in the public interest to allow USF funding requirements to continue to increase, it needs to look to new contribution sources for this funding.⁵⁰

Nextel has no quarrel with the public policy goal of encouraging affordable access to telecommunications services nationwide. However, at some point regulators must recognize that there are better ways of achieving affordable access than by taxing at increasingly higher levels the only carriers that could provide affordable alternatives based on competitive alternatives to former monopoly service providers.

It is undisputed that USF and other funding programs, particularly programs in which the funds are disbursed to specific carriers, distort the functioning of competitive markets.⁵¹ Fundamentally, each decision to fund a service or to move a charge away from an ILEC's interstate access charge recovery requirement and into the USF explicit subsidy pool has a competitive effect. The adverse effect is greatest on carriers such as CMRS providers that largely do not benefit from the program.

⁴⁹ Federal-State Joint Board on Universal Service Seeks Comment on Review of the Definition of Universal Service, *Public Notice*, CC Docket No. 96-45, FCC 01J-1 (rel. Aug. 21, 2001).

⁵⁰ The *Further Notice* suggests that the Commission may consider broadening the base of universal service contributors, and if funding requirements continue to climb, the Commission may well have no alternative but to take this step.

⁵¹ See e.g., Crandall, R. and Waverman, L. *Who Pays for Universal Service? When Telephone Subsidies Become Transparent*, American Enterprise Institute (2000); Rosston, G. and Wimmer, B., *The ABCs of Universal Service: Arbitrage, Big Bucks and Competition*, Stanford Institute for Economic Policy Research Working Paper No. 98-4, April 1999, HASTINGS LAW JOURNAL, Vol. 50, No. 6, August 1999.

Controlling the cost of USF funding requirements on competitors must become a principal regulatory objective of the Commission. The program must not become the equivalent of a regulatory slush fund in which some seek to dump their costs, while profitable fund recipients pocket contributions from carriers that are not even free cash flow positive.

In this instance, the Commission also should immediately consider ending federal USF subsidies for second and third residential lines purchased from incumbent LECs. In the landline residential context, ILECs install the wiring for a second line at the time they install the initial line. There is no reason that competitors ought to pay a fully freighted, embedded cost to the ILEC for their furnishing of luxury service in the form of second and third telephone lines to the same home.⁵²

VII. CONCLUSION

There is no compelling public policy or legal reason for the Commission to adopt broad-based revisions to the USF program at this time. The IXC proposal under consideration would cause dislocation, harm emerging competitors and favor established industry segments. The IXC proposal is not a step towards simplification of the USF assessment program and it is not competitively neutral. It shifts contribution burdens among carrier classes without any regard to the effect on the demand for carrier services or the effect on facilities-based local

⁵² In 1997, when the effective contribution factor was less than 4%, the Commission rejected the Joint Board's proposal to limit USF support to primary residence and to businesses with a single connection. *Federal-State Joint Board on Universal Service, First Report and Order*, 12 FCC Rcd 8776 (1997). Now that carriers are assessed nearly 8% for universal service, the time is ripe for the Commission to revisit this issue, as it proposed to do previously.

telecommunications competition. For all these reasons, the proposal should not be adopted and detailed analysis is required before any connection-based assessment approach could be implemented.

Respectfully submitted,

NEXTEL COMMUNICATIONS, INC.

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April 22, 2002

EXHIBIT 1

Recent IXC Revenue Repor
Recent IXC Revenue Reported in IXC Carrier 10-Q Filings

	AT&T	Sprint	WorldCom
1999	\$46,202,000,000.00	N/A	\$29,586,000,000.00
2000	\$41,623,000,000.00	\$6,040,000,000.00	\$29,456,000,000.00
2001	\$39,964,000,000.00	\$6,715,000,000.00	\$26,701,000,000.00

Recent IXC Revenue Reported in IXC Carrier 10-K Filings

	AT&T	Sprint	WorldCom
1999	\$54,973,000,000.00	\$10,308,000,000.00	\$35,908,000,000.00
2000	\$55,533,000,000.00	\$10,528,000,000.00	\$39,090,000,000.00
2001	\$52,550,000,000.00	\$9,916,000,000.00	\$35,179,000,000.00

I, Cynthia S. Shaw, a legal secretary at Drinker Biddle & Reath LLP do hereby certify that on this 22th day of April, 2002, a copy of the foregoing “**COMMENTS OF NEXTEL COMMUNICATIONS, INC.**” was hand delivered to each of the following:

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